RAILROAD WEEK IN REVIEW
February 5, 2021

"There's been a lot of noise around that [Keystone XL] pipeline for a number of years. We've been able to generate some stable crude-by-rail business out of North Dakota. But I think certainly there is an opportunity for upside if they would move towards shutting it down or putting it on the sideline for a certain amount of time." — John Brooks, Chief Marketing Officer, Canadian Pacific

"Among our covered companies in the railroad space that reported this week, the consensus outlook for 2021 was bullish as trucking capacity remains tight, inventory replenishment continues, and consumer spending is healthy. Carload volume is expected to grow in 2021, with some segments likely outperforming the laggards (coal), which may be positioned to have a strong 2H21." — Jason Seidl, Cowen & Co.

"With respect to the merchandise markets, we expect the steady recovery in manufacturing activity to support our customers' efforts to rebuild inventories and meet increasing demand. Total manufacturing activity is accelerating, driving opportunities across our merchandise segments." — Alan Shaw, Chief Marketing Officer, Norfolk Southern

"Perseverance has been the hallmark of the shortline industry, and as difficult as 2020 was for our industry, it was the year that perseverance paid off on our top legislative priority. After nearly two decades of hard work, 45G, the short line rehabilitation tax credit, was made permanent." — Chuck Baker, President, ASLRRA, in Railway Age

Norfolk Southern in 2020 won new business from 86 customers in seven states. Commodities are all in the merchandise carload sector: pulp and paper, grain, steel and steel scrap, "automotive-related" (parts?), roofing granules, asphalt (STCC 29 in chemicals), and aggregates. NS says in all, customers across 18 states invested $1.8 billion to open new and expanded rail-served facilities. These developments are expected to create more than 54,300 carloads of new rail volume annually.

NS needs this. Merchandise carloads in 2020 accounted for about 27 percent of total volume. Of the 17 commodity groups in the merchandise sector, all but two were down in 2020: farm products ex-grain and waste/scrap — together accounting for three percent of all merchandise carloads. If you include automotive, the broad merchandise category was down more than 13 percent last year.

As an aside, I'd like to think NS short lines are contributing (at one time, NS touted shortline carload and revenue growth). Just in my small community of shortline contacts, we saw in 2020 new carloads of both forest products STCCs, plastics, chemicals, steel, roofing materials, coal, general merchandise for warehousing and distribution in the service area.

Face it. Railroads are hardly in growth mode. Over the past five years 2016-2020 total revenue units on the seven North American railroads are essentially unchanged, though revenue has increased slightly, mainly through rate increases. Operating income is up a bit more as expenses have been cut, and net revenue has gained on below-the-line actions. Long term debt has seen the most CAGR growth of all, though shrinking slightly at CP.

Shortline operator RJ Corman Group has tapped former FRA Administrator Ron Batory for its Board of Directors. Prior to serving at the FRA, Batory had been president of Conrail Shared Assets for more than a dozen years, retiring in 2017. Originally from the midwest, he began railroading the DT&I in 1971.

Batory then served in positions of progressively greater responsibility with the Grand Trunk Western Railroad, the Chicago, Missouri & Western Railway, and Southern Pacific Transportation Company. In 1994, Batory became President of The Belt Railway Company of Chicago. In 2020, *Railway Age* named Batory one of the top 10 Most Influential Leaders in the North American railway industry.

I predict a long and mutually beneficial relationship. R. J. Corman Railroad Group employs approximately 1,500 people in 23 states. In addition to owning and operating short lines, Corman companies provide a broad scope of services to the railroad industry such as emergency response, track material distribution, track construction, industrial switching, and signal design and construction.

The California Transportation Commission (CTC) will distribute $6.45 million to seven shortline railroad infrastructure projects. These are funded through the "2020 Short-Line Railroad Improvement Program" (SLRIP), which was established under California's Short-Line Infrastructure Improvement Act of 2019.

SLRIP provides funds to infrastructure projects intended to "improve freight mobility, volume thresholds, and support modern rail freight traffic and the communities and industries they serve throughout California." The seven projects have a combined value of more than $13 million:

Arizona & California Railroad: Upgrade 3.8 miles of rail and replace 800 tons of ballast. Total project cost: $2,825,560.
Sonoma-Marin Area Rail Transit Rail Freight Improvements, $1,455,850: Repairs to the Black Point Bridge; rehabilitation of two existing freight rail spur; PTC installation. Total project cost: $2,911,700.
Santa Maria Valley Railroad: Replace approximately 1.6 miles of rail as well as ties and ballast. Total project cost: $799,120.
Goose Lake Railway: Replace 1.25 miles of nearly 100-year old rail in the Pit River Canyon. Total project cost: $865,925.

Sacramento Valley Railroad Capacity Expansion: Construct two tracks (1,311 feet in length) to provide additional working/storage capacity for transload business. Total project cost: $1,394,069.
Stockton Terminal & Eastern Railroad: replace and/or repair more than four miles of track. Total cost $1.8 million.

CTC established the 2020 SLRIP as a two-year, $7.2 million program (fiscal years 2020-21 and 2021-22). Since the seven projects only account for $6.45 million, the remaining $750,015 will go into the Trade Corridor Enhancement Account, according to CTC.

Due to requirements of the SLRIP, projects were restricted to Caltrans and the Regional Transportation Planning Agencies. The SLRIP funds could not be allocated to a private entity. Additionally, projects must begin construction by Dec. 31, 2022.

Kudos to the CTC for initiating these projects. I'm familiar with a number them and feel certain customers and the community will benefit from more efficient railroad infrastructure. Would that more states were as aggressive.

CSX gets a "C" or Hold rating on the Schwab Equity Rating scale, which looks at five areas of share performance: growth, quality, sentient, and valuation. CSX is rated "neutral" in all but Quality, which is "of high importance in the scoring system," and where CSX is scored Negative.

The Quality score is "based on a number of operating performance measures derived from recent financial statement data. Stocks with attributes such as high profitability, high earnings quality, conservative investment spending and better operating efficiency tend to have better Quality scores. Highly-rated stocks within this category may have the potential for price appreciation, as investors perceive that these companies have the financial strength to potentially grow earnings faster than their peers." CSX does not make Schwab's cut.

Similarly, 15 of 25 sell-side analysts traced by Yahoo rank CSX as Hold. Yet the half -dozen analyst reports I see have CSX increasing 2021 earnings by more than 20 percent mainly due to lower operating expenses. To me, revenue unit growth is key, because without revenue you can't grow earnings. Here, the CSX track record is poor. Over the past five years 2016-2020 CSX carloads saw a CAGR of -1.5 percent and revenue -0.9 percent. Color me skeptical of CSX growing earnings by 20 percent in 2021.